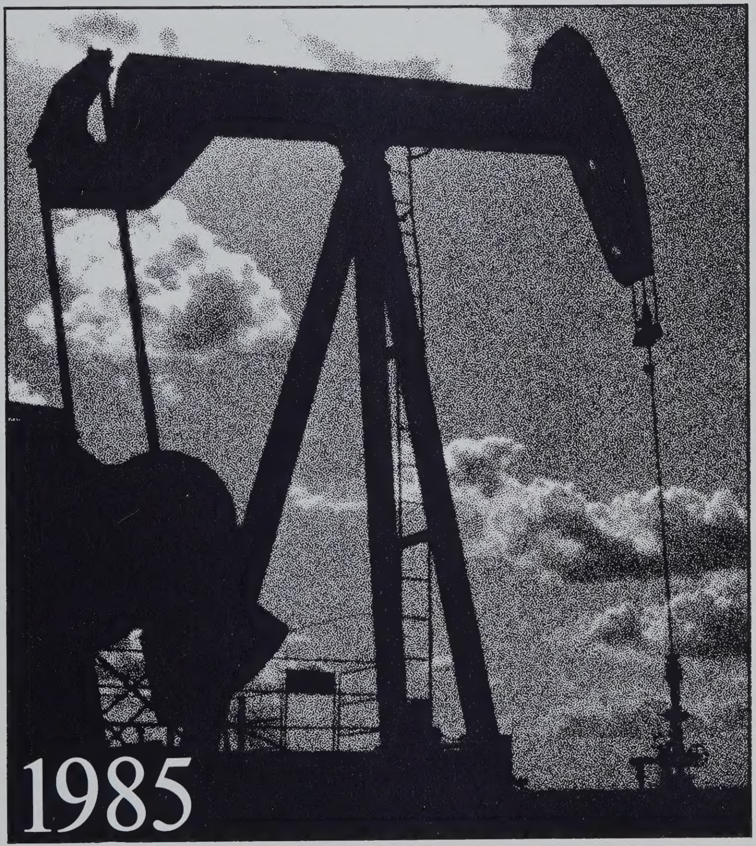
BRANA
OIL & GAS LTD.



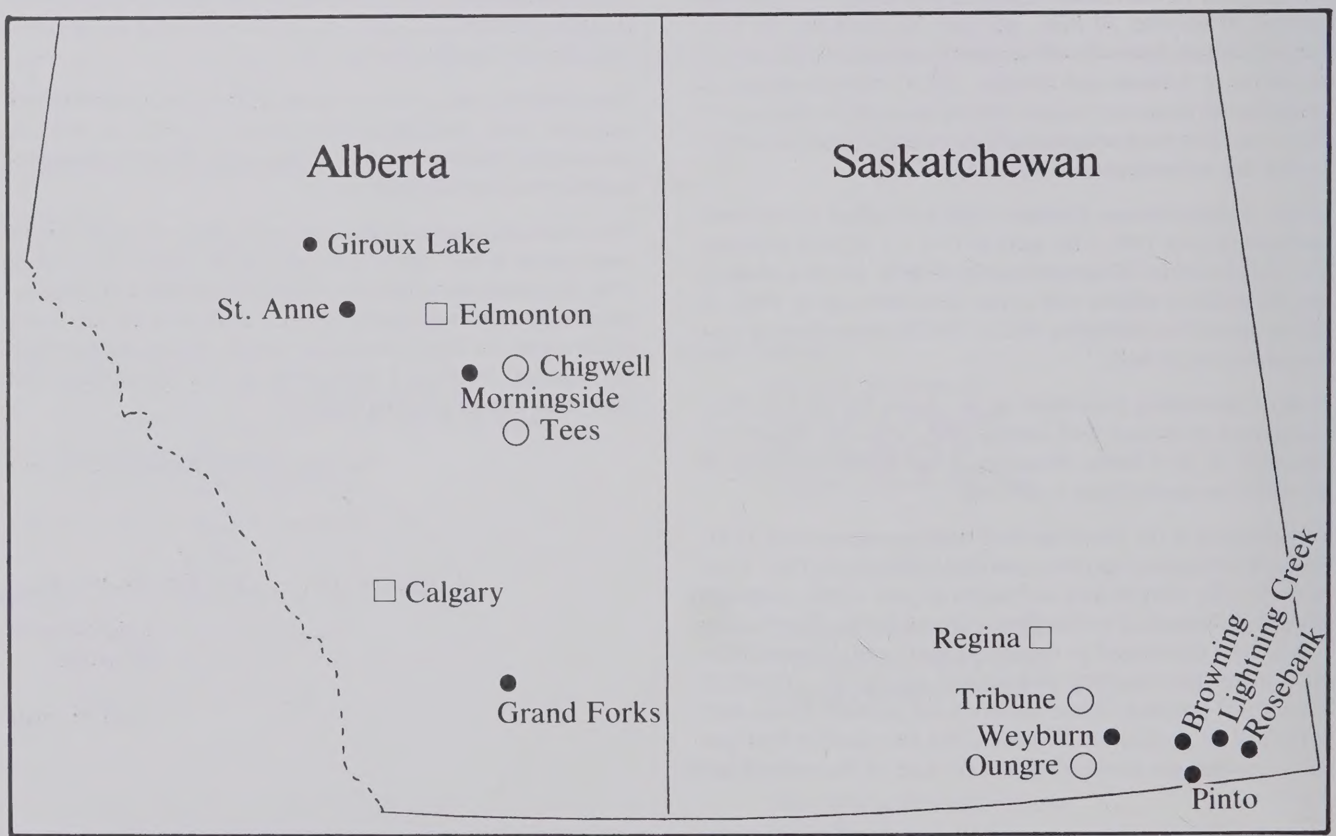
ANNUAL REPORT

Exploration Activity & Summary of Operations

1985 DRILLING RESULTS

	Gross Wells	Gross Oil Wells	Gross Suspended or D & A	Brana Net W.I. (%)
ALBERTA				
Morningside/Ponoka	4	4	—	*
Grand Forks	1	1	—	*
TOTAL	5	5	—	*

* Various minor interests.



Brana's level of drilling activity declined dramatically during 1985. This decrease is due to the initiation of internally generated prospects and the Company's decision to spread risk through the farmout of the test well on each new prospect. This strategy saw successful oil wells drilled at Pinto, Saskatchewan and Giroux Lake, Alberta.

All of the wells in which Brana holds an interest receive NORP pricing.

The Company did not participate in any projects in the United States during 1985.

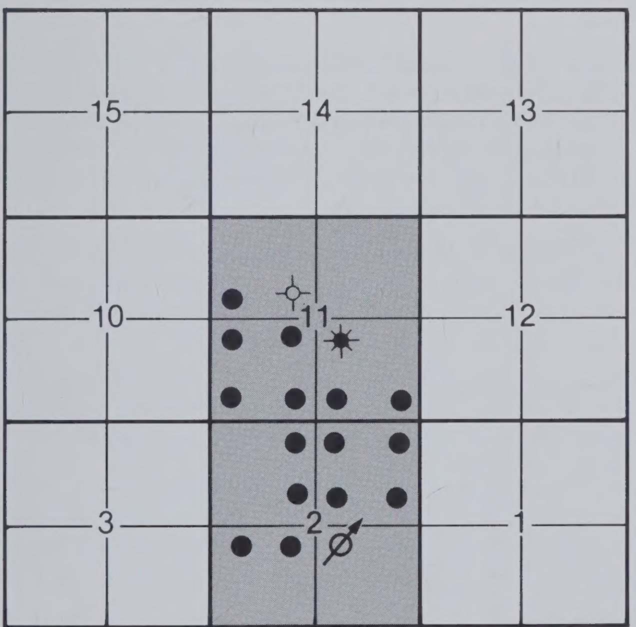
ALBERTA

St. Anne

The St. Anne property is now fully drilled. A study to evaluate the feasibility of waterflooding the Banff formation is expected to be finished late in the first quarter or early in the second quarter of 1986. However, with the recent declines in the world price of crude oil, we anticipate that implementation of any waterflood project will be deferred.

The G.O.R. penalties placed on several of the St. Anne wells by the Energy Resources Conservation Board have yet to be lifted. These penalties and low selling prices for 18° to 21° A.P.I. oil will reduce 1986 revenue from St. Anne dramatically and also cause it to be intermittent in production.

Brana continues to hold 2.5% or 3% working interests in this project.



ST. ANNE FIELD

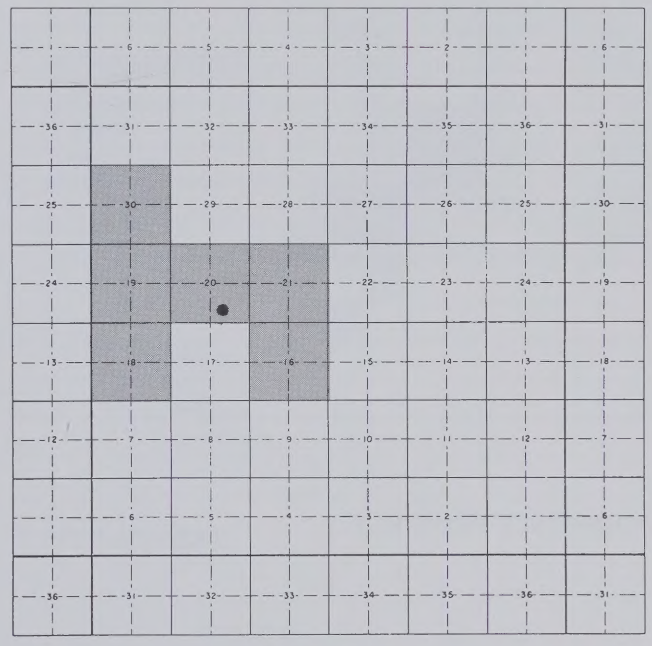
LEGEND

- ● Oil Well in which Brana has a working interest
- ☼ Gas Well
- ⌀ Service Well
- ⌖ Dry Hole
- ▭ Brana Oil & Gas Lands

Giroux Lake

Brana purchased an 8% working interest in 640 acres of Crown land in July 1985. This acreage was subsequently farmed out and a Viking "C" oil well was drilled in November 1985. Brana holds a G.O.R.R. convertible at payout of the 2-20-66-21 W5M well to 3.4% working interest.

The Company has participated to its 3.4% W.I. in the subsequent acquisition of 5 section of offsetting Crown land. Two or three development wells will be drilled in the summer of 1986 to offset the 2-20 well that has flowed an average of approximately 50 barrels per day of clean oil since November 1985.



GIROUX LAKE PROSPECT

Morningside/Ponoka

The Company now holds various minor interests in 14 gross wells in this project. Four wells are gas wells with condensate production potential, nine are gassy oil wells and one is suspended.

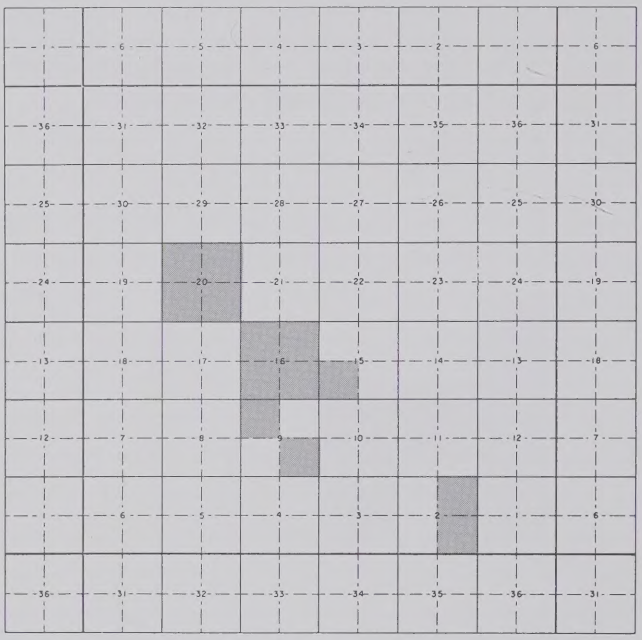
Recent discussions with Morgan Hydrocarbons Ltd. and D.M. Wolcott & Associates Ltd., the operators of this project, have indicated that A.F.E.'s have been prepared to construct a gas gathering system and a compression and NGL extraction facility at a total gross cost of $7.0 million. Brana will participate in the plant facilities and will benefit from sales of its share of the natural gas & NGL produced but also from the custom processing of third party gas.

Good Production Practise status, subject to completion of the capital facilities, has been approved. This will allow the oil production from the Morningside/Ponoka project to increase by approximately 50% upon plant start-up.

Due to the capital facility plans and the drilling of four new development wells, Brana decided to not sell this project interest under the offer received from D.M. Wolcott & Associates Ltd. in October, 1985.

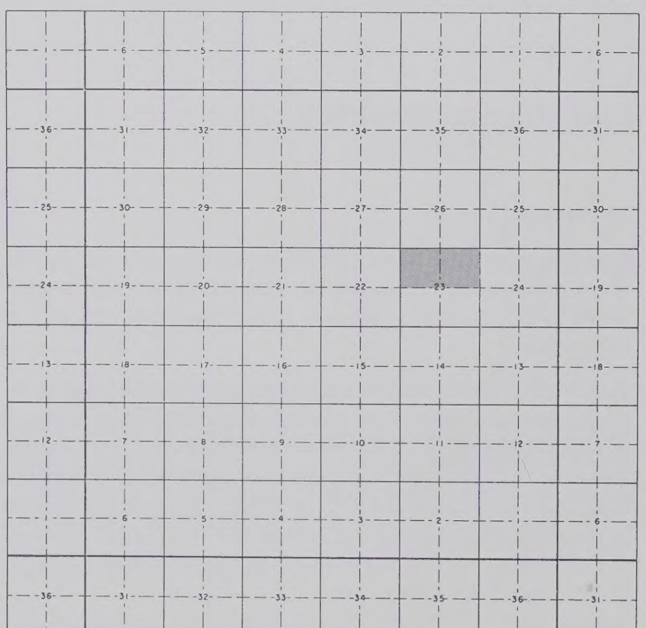
Chigwell

Brana holds a 20% working interest in 320 acres of freehold lands and working interests ranging from 6.3% to 10% in 1760 acres of Crown land in Township 41, Range 24 W4M. Locations in 8-2, 11-9 and 15-20 would test three separate Nisku structures. The Company is currently soliciting farm-in proposals.



CHIGWELL PROSPECT

TEES PROSPECT



Tees

Brana holds a 20% working interest in the freehold lands comprising N½ Section 23-40-24 W4M. The acreage acquisition was based on geological interpretation of oil shows in three adjoining dry holes and on seismic shot by the Company in 1985. A potential location in Lsd. 14 would test the Nisku structure.

Other Alberta Projects

As at year end 1984, Brana held minor working interests in two wells in the Grand Forks area capable of total initial daily production rates of 500 barrels of fluid with a 7% water cut. One development location was drilled at Grand Forks in early 1985 and is an indicated oil well.

Brana holds interests in oil wells at Hays, Nipisi and Virginia Hills, as well as a dual zone gas well at Gull Lake and another gas well at Whitecourt.

All of the "Other Alberta Projects" and the Morningside/Ponoka wells were part of a program initiated by D. M. Wolcott & Associates Ltd. The Company has invested $100,000 in this program prior to APIP incentives.

SOUTHEAST SASKATCHEWAN

Pinto

Under the farmout agreement reached in late 1984, a well in Lsd. 14-2-1-5 W1M was drilled in June 1985. A follow-up well in Lsd. 16 was drilled in January 1986. The discovery well is pumping at approximately 15 barrels per day with the 16-2 well flowing approximately 25 barrels per day of clean oil without reservoir stimulation.

The Saskatchewan Crown has approved 80 acre spacing for this land, however, further drilling will not occur until oil prices stabilize or the capital costs associated with drilling additional wells decline dramatically.

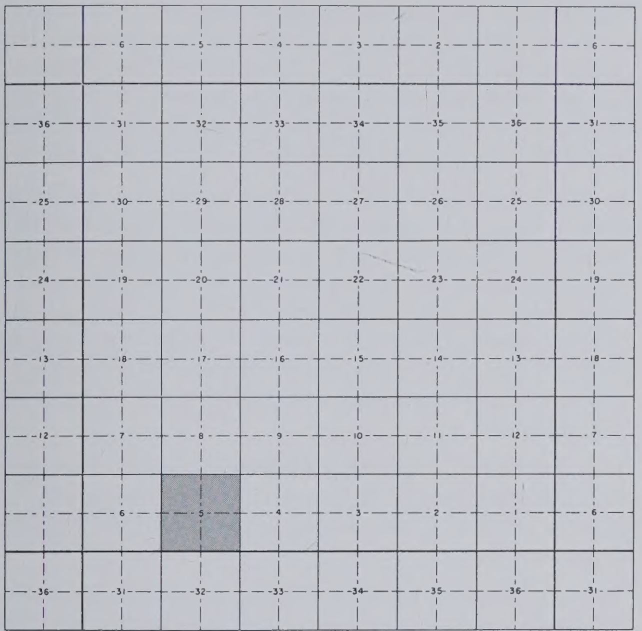
Brana holds a G.O.R.R. convertible to a 3.5% working interest after payout in each of the existing wells, and will participate to its 3.5% W.I. in subsequent development drilling.

PINTO PROSPECT

Oungre

Brana holds a 10% working interest in the 640 acres of this prospect that was acquired from the Crown based on interpretation of new seismic shot by the Company.

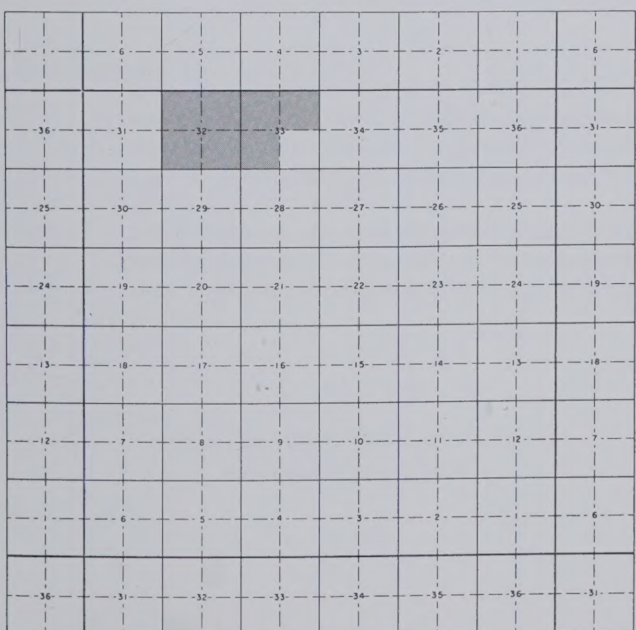
There are no current plans for drilling this acreage.



OUNGRE, SASKATCHEWAN

Tribune

During 1985, Brana participated to a 10% working interest at Crown land sales to acquire the 1120 acres of this prospect. Recent seismic detailing has followed up the initial seismic work in which Brana participated, and locations in 8-32 and 5-33 have now been identified. Attempts are being made to find farm-in partners to drill the first well on this prospect.



TRIBUNE, SASKATCHEWAN

UNDEVELOPED LAND HOLDINGS, at December 31, 1985

ALBERTA	Gross Acres	W.I. (%)	Net Acres
Chigwell	320	20.0	64.00
	640	6.3	40.32
	1,120	10.0	112.00
Giroux Lake	3,840	3.4	130.56
Tees	320	20.0	64.00
	Total Alberta		410.88

SASKATCHEWAN	Gross Acres	W.I. (%)	Net Acres
Oungre	640	10.0	64.00
Pinto	640	10.0	64.00
Tribune	1,120	10.0	112.00
	Total Saskatchewan		240.00
	Grand Total		650.88

Financial Review

Revenue from oil sales increased 17% to $315,298 from the 1984 revenue level of $269,355. Funds provided from operations decreased slightly to $149,954 from the level of $151,288 achieved in 1984, with net after tax earnings of $24,454 or $0.018 per share, a decline of $33,834 over the 1984 performance.

As discussed earlier in this report, Brana drilled very few new wells during 1985, with the production increases due principally to the start-up of solution gas sales at St. Anne, and a full year's production revenue for the Ponoka/Morningside project. The increased production and royalty expenses incurred during 1985 are the direct result of higher production levels.

During 1985, Brana continued a policy of minimizing General and Administrative type expenses, with total costs incurred of $41,039. This total includes the cost of having engineering studies prepared on the St. Anne & S.E. Saskatchewan projects, with the remaining expenses directly related to being a public company.

By December 31, 1984, Brana had incurred a working capital deficit of $14,639, a decrease of $158,370 from the 1983 year end position. Steps were taken during 1985 to remedy this position and year end 1985 showed an improved net working capital of $69,491. This improvement is due principally to the sale of certain undrilled lands and marginal wells in S.E. Saskatchewan, the proceeds from which paid debts to the program operator in full.

The Company had initially intended to also sell the Morningside/D.M. Wolcott Program interest with proceeds to have repaid bank debt. However, reassessment of the project in October 1985 indicated that participation in further development drilling and the gas gathering, and liquids extraction system would be far more profitable for Brana in the long term.

As previously discussed herein and in previous quarterly reports, Brana has created four subsidiary companies. The intention of this project is to distribute the shares of these companies on a one share for every one Brana share held basis. However, the Company is not legally empowered to do this until approval from the Alberta Securities Commission (ASC) is obtained. Prospectus covering each of the four subsidiaries were filed on January 31, 1986 to obtain the required ASC approvals.

The creation of subsidiaries will allow Brana to attract new assets, cash injections or businesses into the companies without massive dilution to the ownership position of the existing Brana shareholders.

These subsidiaries and the $47,923 spent on land acquisitions on new oil prospects are the basis for future growth and continued improvement in the financial strength of the Company.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Brana Oil & Gas Ltd. as at December 31, 1985 and the consolidated statements of earnings and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at December 31, 1985 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada
April 28, 1986

VENNARD JOHANNESEN & CO.
Chartered Accountants

BRANA
Oil & Gas Ltd.

Consolidated Balance Sheet

As At December 31, 1985

CONSOLIDATED BALANCE SHEET

	1985 $	1984 $
ASSETS		
Current		
Cash	**16,747**	4,175
Accounts receivable (Note 2)	**98,594**	57,660
Drilling advances	**5,309**	49,465
	120,650	111,300
Petroleum Properties	**682,595**	685,771
Other Assets	**16,000**	nil
	819,245	797,071
LIABILITIES		
Current		
Accounts payable	**47,002**	107,269
Funds held in trust (Note 5)	**4,157**	18,670
	51,159	125,939
Long-Term Debt (Note 4)	**150,000**	100,000
Deferred Income Taxes	**40,500**	18,000
	241,659	243,939
SHAREHOLDERS' EQUITY		
Capital Stock (Note 5)	**489,830**	489,830
Retained Earnings	**87,756**	63,302
	577,586	553,132
	819,245	797,071

See accompanying notes

APPROVED BY THE DIRECTORS

Director

Director

BRANA
Oil & Gas Ltd.

Consolidated Statement of Earnings and Retained Earnings

For The Year Ended
December 31, 1985

CONSOLIDATED STATEMENT OF EARNINGS AND RETAINED EARNINGS

	1985 $	1984 $
Revenue		
Production	**315,298**	269,355
Interest	**1,269**	5,792
	316,567	275,147
Expenses		
Depletion	**115,000**	75,000
Production	**70,038**	59,513
Royalties	**58,378**	56,044
Audit and accounting	**20,339**	10,016
Shareholder relations	**5,695**	7,420
Interest	**13,158**	4,310
Office	**2,490**	3,124
Trustee fees	**1,420**	2,118
Legal and engineering	**11,095**	1,163
Promotion	**—**	1,151
	297,613	219,859
Earnings Before Income Taxes and Minority Interest	**18,954**	55,288
Income Taxes		
Alberta royalty tax credit	**16,000**	21,000
Deferred income taxes	**(22,500)**	(18,000)
	(6,500)	3,000
Minority Interest	**12,000**	—
Net Earnings for the Year	**24,454**	58,288
Retained earnings — beginning of year	**63,302**	5,014
Retained Earnings — End of Year	**87,756**	63,302
Earnings per share	**.018**	.044
Earnings per share — fully diluted	**.013**	.032

See accompanying notes

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	1985 $	1984 $
Source of Funds		
Operations		
Net earnings for the year	**24,454**	58,288
Add items not requiring an outlay of funds		
Depletion	**115,000**	75,000
Deferred income taxes	**22,500**	18,000
Minority interest	**(12,000)**	—
	149,954	151,288
Long-term debt	**50,000**	100,000
Common shares issued	—	93
Sale of petroleum properties	**95,723**	—
	295,677	251,381
Use of Funds		
Petroleum properties	**211,547**	409,751
Increase (Decrease) in Working Capital	**84,130**	(158,370)
Working capital (deficiency) — beginning of year	**(14,639)**	143,731
Working Capital (Deficiency) — End of Year	**69,491**	(14,639)

See accompanying notes

Consolidated Statement of Changes in Financial Position

For The Year Ended December 31, 1985

BRANA
Oil & Gas Ltd.

Notes to the Consolidated Financial Statements

For The Year Ended
December 31, 1985

1. Significant Accounting Policies

Basis of consolidation —

The Company's financial statements include the accounts of the Company and its 80% owned subsidiaries, BOL Energy Ltd., Cable Hydrocarbons Inc., Marker Resources Co. Ltd., and Post Petroleums Limited.

Oil and gas operations —

The Company follows a form of full cost accounting for oil and gas operations whereby all costs of exploring and developing oil and gas reserves are capitalized. Such costs include land acquisition costs and geological and geophysical expenses. In addition, the cost of drilling both productive and non-productive wells, and overhead expenses related to exploration activities are capitalized.

The carrying value of the Company's oil & gas properties is limited to the amount determined by estimating the present value of future net revenues from proven reserves together with the value of unproven reserves at the lower of cost or net realizable value.

The accumulated costs together with estimated future capital costs associated with proven reserves, are depleted by the unit of production method which is based on production and estimated proven reserves of oil and gas as determined by independent consultants. In calculating depletion, natural gas reserves and production are converted to equivalent barrels of oil. Proceeds on disposal of properties are ordinarily deducted from accumulated costs without recognition of gain or loss. Any gain or loss realized on the disposition of a major property would be recognized in the statement of earnings.

Joint venture accounting —

Substantially all of the Company's exploration and production activities related to oil and gas are conducted jointly with others and accordingly the accounts reflect only the Company's proportionate interest in such activities.

Income taxes —

The interperiod tax allocation basis of accounting is used with respect to all differences between the time when costs and revenues are recognized for income tax purposes and when they are recorded for book purposes.

Government Incentive Grants —

Grants received under the Petroleum Incentives Program are applied against associated drilling costs prior to the calculation of the depletion allowance.

Earnings per share —

Net earnings per share was calculated by dividing net earnings by the weighted average number of shares outstanding during the year.

The fully diluted earnings per share calculation is based on the assumption that share purchase options were exercised at the date of issuance and the funds received therefrom were invested at an annual rate of 10%.

2. Accounts Receivable

Accounts receivable consists of the following:

	1985 $	1984 $
Trade receivables	**71,693**	5,967
Government drilling incentives	**7,142**	20,891
Alberta royalty tax credit	**19,759**	30,802
	98,594	57,660

3. Petroleum Properties

	1985			1984
	Cost $	Accumulated Depletion $	Net Book Value $	Net Book Value $
Canadian petroleum and natural gas properties	**884,995**	**202,400**	**682,595**	685,771

4. Long-term Debt

The long-term debt consists of a demand loan bearing interest at the bank prime rate plus ½ of 1%. The loan is secured by a general assignment of accounts receivable and a pledge to not encumber or sell the petroleum and natural gas properties without the Bank's consent. Subsequent to year end the authorized amount of the loan was increased to $200,000 and arrangements were made whereby the authorized amount would be reduced by $4,200 per month. At December 31, 1986, the authorized amount will exceed $150,000.

The required future repayments are:

1987	$46,600
1988	50,400
1989	50,400
1990	2,600

5. Share Capital

(a) Authorized

The company has authorized an unlimited number of common voting, common non-voting, and preferred shares, all without nominal or par value.

(b) Issued

	1985 $	1984 $
1,330,259 Common voting shares	**489,830**	489,830

Pursuant to the flow through share agreement of October 5, 1983, investors placed $225,000 in trust with the Company. Expenditures of these funds on drilling activity earned common voting shares of the Company at a rate of 1 share for each $.60 of expenditure.

At December 31, 1985, all shares with respect to this agreement have been issued and there remains $4,157 of unexpended funds held in trust which is to be returned to one of the investors under the terms of the agreement.

(c) At a meeting of the Board of Directors held on April 24, 1984, share purchase options for the directors totalling 500,000 shares were authorized. One-half of these options are exercisable at $.50 per share, with the balance at $.75 per share. The options will expire May 1, 1989.

6. Remuneration of Directors and Senior Officers

No remuneration was paid to the directors and officers of the Company as defined in the Alberta Business Corporations Act.

Notes to the Consolidated Financial Statements

(continued)

7. Income Taxes

The difference between the expense recorded and the expected tax expense obtained by applying the statutory Canadian income tax rate to earnings before taxes is summarized as follows:

	1985 $	1984 $
Expected Tax Expense	**8,900**	25,800
Crown Royalties	**25,300**	21,600
Alberta Royalty Tax Credit	**(16,000)**	(21,000)
Resource allowance	**(21,000)**	(23,000)
Depletion on costs with no tax basis	**9,300**	(6,400)
	6,500	(3,000)

8. Business Combination

On October 8, 1985, the Company purchased 80% of the outstanding shares of four newly formed oil & gas exploration companies: BOL Energy Ltd., Cable Hydrocarbons Inc., Marker Resources Co. Ltd., and Post Petroleums Ltd. These acquisitions have been accounted for by the purchase method. The results of operations of these four subsidiaries since October 8, 1985 have been included in these financial statements on a consolidated basis.

Net assets acquired at October 8, 1985 are summarized as follows:

Working capital	$60,000
Other assets	16,000
	76,000
Minority interest	(12,000)
Purchase consideration (cash)	$64,000

9. Subsequent Event

During the year, the Company evaluated the carrying value of its oil and gas properties by estimating the present value of future net revenues from production of its reserves. These estimates involved underlying assumptions regarding the future selling prices of crude oil and natural gas. Subsequent to year end, the price of oil fell significantly below the prices used in the Company's evaluations. Based on a Cdn. $20.00/bbl value, the carrying value of petroleum properties would be reduced by $200,000. This write-down will be reflected in the first quarter financial results of the Company.

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